


Lornex

MINING CORPORATION LTD.

ANNUAL REPORT 1977



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OFFICERS	Honorary Chairman E. H. LORNTZSEN Chairman and Chief Executive Officer R. D. ARMSTRONG President and Chief Operating Officer G. R. ALBINO Treasurer J. VAN NETTEN Secretary C. W. M. BURGE
DIRECTORS	G. R. ALBINO, Mississauga, Ontario W. A. ARBUCKLE, Montreal R. D. ARMSTRONG, Don Mills, Ontario A. FUJISAKI, Tokyo, Japan R. A. HAMMOND-CHAMBERS, Edinburgh, Scotland N. B. IVORY, Montreal E. H. LORNTZSEN, Vancouver A. F. LOWELL, Islington, Ontario H. A. PAKRUL, Mississauga, Ontario J. HERBERT SMITH, Toronto J. VAN NETTEN, Willowdale, Ontario R. W. WRIGHT, CBE, London, England
HEAD OFFICE	580 Granville St. Vancouver
MINE OFFICE	P.O. Box 1500 Logan Lake
AUDITORS	Coopers & Lybrand Vancouver
REGISTRAR AND TRANSFER AGENT	National Trust Company, Limited Vancouver
SHARES LISTED	Vancouver Stock Exchange
THE ANNUAL GENERAL MEETING	11:00 a.m., Thursday, April 20, 1978 Shuswap Lake Room, The Four Seasons Hotel, 791 West Georgia Street, Vancouver, British Columbia.

Giant operations require giant equipment.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Net earnings for the year 1977 were \$7,781,000 or \$0.94 per share compared to \$15,903,000 or \$1.93 per share for the year 1976. The decline in net earnings was due primarily to lower copper prices. In addition, production of copper in concentrate was slightly below that of the previous year and expenses were higher.

Comparative milling, metallurgical, production and shipping data for the years 1977 and 1976 are as follows:

	1977	1976
Tons of ore milled (thousands)	17,065	17,016
Average tons milled per operating day	46,753	46,877
Average millhead grade		
— copper	0.481%	0.511%
— molybdenum	0.015%	0.016%
Average mill recovery		
— copper	88.9%	86.7%
— molybdenum	72.2%	69.7%
Pounds of payable metal in concentrate produced (thousands)		
— copper	141,111	145,712
— molybdenum	3,795	3,769
Pounds of payable metal in concentrate delivered (thousands)		
— copper	153,792	144,301
— molybdenum	4,071	3,782

The decline in production of copper in concentrate from 145.7 million pounds in 1976 to 141.1 million pounds in 1977 was due to the slightly lower average mill head grade of ore. The gross copper revenue price per payable pound for the year averaged 60 cents as compared to 65 cents in 1976 but the impact of the lower prices for copper was modified somewhat by higher prices for molybdenum. The overall effect was that net revenue from mine production, comprising revenue from copper, molybdenum and minor values of precious metals less smelting, refining and marketing charges, decreased to \$75,449,000 in 1977 from \$82,940,000 in 1976. The method by which revenue from mine production is determined is described in the Accounting Policies section of this Report.

As previously reported it had been agreed with the Japanese buyers of the copper concentrates that Lornex would negotiate during the first quarter of 1977 the refining charges to be deducted from the selling price of shipments made subsequent to March 31, 1977. These negotiations were concluded in August, 1977 and agreement was reached whereby refining charges were increased for the period April 1, 1977 to March 31, 1979.

An aggressive cost control program was continued throughout the year; however, costs of operating materials and supplies continued to escalate. The total quantity of ore milled was virtually unchanged compared to the previous year but in the normal course of pit development the ratio of waste material handled to ore mined increased by about 32%. Despite this the number of employees was maintained at about the same level as in 1976. The increase in amortization and depreciation charged in 1977 is mainly related to the new pit equipment which has been purchased since September, 1976.

Net capital expenditures in 1977 were \$18,584,000. The major items were construction of the new tailings dam, purchase of new 235 ton capacity trucks and rebuilding part of the original 120 ton capacity truck fleet, construction of pit services buildings and a new warehouse, and normal equipment replacements. The program to increase the capacity of some equipment used in the open pit operation, commenced in 1976 and comprising purchase of new equipment and rebuilding of other equipment, was largely completed by the end of 1977. It is expected that capital expenditures for 1978 and immediately succeeding years will be significantly lower than the expenditures of \$18.6 million in 1977 and \$17.1 million in 1976.

As previously reported Lornex repaid \$71 million comprising Income Debenture debt and accrued interest thereon on September 30, 1976 mainly from the proceeds of new bank loans, in the amount of U.S. \$70 million, which are repayable semi-annually over a five year term. Repayments totalling U.S. \$14 million were made in 1977 and a third repayment of U.S. \$7 million was made in February, 1978 reducing the balance currently outstanding to U.S. \$49 million.

The Company continues to be subject to the provisions of the Federal Government's Anti-Inflation Act and Regulations, which became effective October 14, 1975, controlling prices, profit margins, compensation to employees and dividends to shareholders. As concentrate sales are made entirely to export markets, Lornex' prices and profit margins are exempt from regulatory controls; however, compensation is subject to these controls. Amendments to the Anti-Inflation Act have been introduced by the Federal Government to provide for a phased decontrol program to commence on April 14, 1978. Since collective agreements with the production and maintenance and office and technical employees, as amended to comply with Anti-Inflation Board decisions, will expire on June 30, 1978, the contracts negotiated after that date will not be subject to compensation controls.

Lornex, Canada's largest base metals mine, turned in a good performance in a depressed copper market.



235-ton-capacity truck hauls ore from the Lornex open pit to primary crusher.

Mechanics are dwarfed by truck tires.



Youngsters frolic in pond at Logan Lake, where most Lornex employees reside.

During the year Mr. C. W. Reno, who was General Manager of Lornex and a Director and Vice-President of the Company, resigned to take up a position in another country. Mr. L. H. Hunter, Operations Manager, who has been with the Lornex organization since 1973, was appointed to the position of Mine Manager.

Mr. W. A. Arbuckle has reached retirement age under the Company's policy and accordingly will not present himself for re-election as a Director. Mr. Arbuckle became a Director of the Company in 1966 and served in this capacity during the period in which the Lornex mine and mill were brought into successful commercial production and up to the present time. His fellow directors wish to record their appreciation for the contribution which he made to the Company's affairs throughout this period.

It is intended that Dr. D. S. R. Leighton, Director of The Banff Centre, and Mr. Ian F. Rushbrook, Director of Ivory &

Sime Limited, Investment Managers, will be elected to the Board at the Annual General Meeting on April 20, 1978.

The Directors of the Company wish to record their appreciation of the loyal and diligent efforts of all the individuals who contributed so substantially to the Company's successful operations during 1977.

On behalf of the Board.

R. D. ARMSTRONG,
Chairman and
Chief Executive Officer

G. R. ALBINO,
President and
Chief Operating Officer

Vancouver, B.C.
February 21, 1978

Auditors' Report to the Shareholders

We have examined the statement of financial position of Lornex Mining Corporation Ltd. as at December 31, 1977, and the statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the company as at December 31, 1977, and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Vancouver, British Columbia
February 2, 1978

COOPERS & LYBRAND
Chartered Accountants

ACCOUNTING POLICIES

The principal accounting policies followed by Lornex Mining Corporation Ltd. are summarized hereunder:

REVENUE FROM MINE PRODUCTION AND VALUATION OF CONCENTRATES AWAITING SHIPMENT

Production is valued and taken into income as revenue from mine production at estimated realizable metal prices less provision for possible fluctuation in price; concentrates awaiting shipment are also valued on this basis. Adjustments are made to revenue from mine production with respect to concentrate shipments when the actual metal price is known and the final weight and assay adjustments are determined. Estimated smelting, refining and marketing charges are accrued at time of production and these charges are also adjusted with respect to shipments when the final weight and assay adjustments and marketing charges are determined.

At December 31, 1977 inventories of 22.3 million payable lbs. of copper and 0.5 million payable lbs. of molybdenum contained in concentrates awaiting shipment were valued as described above; in addition, shipments totalling 6.2 million payable lbs. of copper for which the final price has not been established were also priced in this manner and the values are included in settlements receivable.

CONVERSION OF UNITED STATES CURRENCY

The accounts in United States currency are stated in Canadian dollars on the following basis:

Current assets and current liabilities at year-end exchange rates; all other assets and long term liabilities at rates in effect at time of transactions, and revenues and expenses at actual rates prevailing during the year.

MINE SUPPLIES

Mine supplies are valued at average cost.

DEPRECIATION AND AMORTIZATION

Depreciation is provided on mining equipment on a straight-line basis over the shorter of its physical life or the estimated life of the mine. The cost of plant and equipment, mining properties and preproduction expenditures is amortized on a unit-of-production basis over the estimated life of the mine.

INCOME AND MINERAL RESOURCE TAXES

The Company provides for deferred income and mineral resource taxes on all significant timing differences which represent the tax effects of revenue and expense items reported for tax purposes in periods different than for accounting purposes.

Statement of Financial Position

DECEMBER 31, 1977

(\$000's omitted)

CURRENT ASSETS:	1977	1976
Cash and short term deposits	\$ 11,216	\$ 19,825
Accounts and settlements receivable and prepaid expenses (note 4)	14,257	8,797
Concentrates awaiting shipment (note 4)	13,201	20,985
Mine supplies (note 4)	9,974	10,185
Total	48,648	59,792
Less:		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	12,768	12,271
Payable to Rio Algom Limited	137	239
Income and mineral resource taxes payable	1,904	5,721
Long term debt due within one year (note 4)	7,630	7,070
Total	22,439	25,301
WORKING CAPITAL	26,209	34,491
Plant and equipment, less depreciation (note 2)	109,381	97,990
Mining properties and preproduction expenditures, less amortization (note 3)	37,781	39,660
	147,162	137,650
TOTAL ASSETS LESS CURRENT LIABILITIES	173,371	172,141
Deduct:		
Long term debt (note 4)	48,851	62,263
Deferred income and mineral resource taxes	35,326	28,535
	84,177	90,798
EXCESS OF ASSETS OVER LIABILITIES	\$ 89,194	\$ 81,343
OWNERSHIP EVIDENCED BY:		
Capital stock (note 5)		
Authorized –		
9,500,000 common shares, par value of \$1.00 each		
4,500,000 Class A shares, par value of \$1.00 each		
Issued –		
8,261,162 common shares (8,253,062 shares in 1976)	\$ 8,261	\$ 8,253
Premium less discount on shares issued for cash (includes \$62 premium on shares issued under stock option plan in 1977 and \$175 in 1976)	3,259	3,197
Retained earnings	77,674	69,893
Total	\$ 89,194	\$ 81,343

Approved on behalf of the Board:

NEIL B. IVORY, Director

R. D. ARMSTRONG, Director

Statement of Earnings

YEAR ENDED DECEMBER 31, 1977

(\$000's omitted)

	1977	1976
REVENUE:		
Net revenue from mine production	\$ 75,449	\$ 82,940
Investment and other income	1,495	1,503
	<u>76,944</u>	<u>84,443</u>
EXPENSES:		
Operating costs	39,788	33,572
Administrative and general expenses	7,564	6,913
Amortization and depreciation	9,072	8,002
	<u>56,424</u>	<u>48,487</u>
Operating profit	20,520	35,956
Interest on long term debt	5,139	5,990
Earnings before taxes	<u>15,381</u>	<u>29,966</u>
Income and mineral resource taxes		
— Current	250	3,963
— Deferred	7,350	10,100
	<u>7,600</u>	<u>14,063</u>
NET EARNINGS FOR THE YEAR	<u>\$ 7,781</u>	<u>\$ 15,903</u>
NET EARNINGS PER SHARE	<u>\$ 0.94</u>	<u>\$ 1.93</u>

Statement of Retained Earnings

YEAR ENDED DECEMBER 31, 1977

(\$000's omitted)

	1977	1976
BALANCE, beginning of year	\$ 69,893	\$ 53,990
Net earnings for the year	7,781	15,903
BALANCE, end of year	<u>\$ 77,674</u>	<u>\$ 69,893</u>

Statement of Changes in Financial Position

YEAR ENDED DECEMBER 31, 1977

(\$000's omitted)

SOURCE OF FUNDS:	1977	1976
Operations		
Net earnings for the year	\$ 7,781	\$ 15,903
Add charges against earnings not involving current outlay of funds:		
Amortization and depreciation	9,072	8,002
Deferred income and mineral resource taxes	7,350	10,100
Interest on Income Debentures	—	4,330
Total funds from operations	24,203	38,335
Bank loans (U.S. \$70,000)	—	68,183
Housing loans (net)	225	630
Issue of common shares under stock option plan	70	202
	<u>24,498</u>	<u>107,350</u>
DISPOSITION OF FUNDS:		
Expenditures on plant and equipment (net)	18,584	17,115
Recoverable royalties	559	1,955
Reduction of long term debt:		
Bank loans (1977 — U.S. \$14,000; 1976 — U.S. \$7,000)	13,637	6,818
Repayment of Income Debentures and accrued interest	—	71,013
	<u>32,780</u>	<u>96,901</u>
INCREASE (DECREASE) IN WORKING CAPITAL	(8,282)	10,449
WORKING CAPITAL, beginning of year	<u>34,491</u>	<u>24,042</u>
WORKING CAPITAL, end of year	<u>\$ 26,209</u>	<u>\$ 34,491</u>

Notes to the Financial Statements

DECEMBER 31, 1977

1. ACCOUNTING POLICIES

The information on page 6 presents a summary of certain accounting policies and is an integral part of these financial statements.

2. PLANT AND EQUIPMENT

	1977	1976
Plant and equipment at cost	\$140,930,598	\$122,939,728
Less accumulated depreciation	31,549,765	24,949,351
	<u>\$109,380,833</u>	<u>\$ 97,990,377</u>

3. MINING PROPERTIES AND PREPRODUCTION EXPENDITURES

	1977	1976
Mining properties at cost	\$ 1,233,179	\$ 1,233,179
Less accumulated amortization	214,829	173,874
	<u>1,018,350</u>	<u>1,059,305</u>
Preproduction expenditures at cost	46,213,277	46,213,477
Less accumulated amortization	9,450,329	7,612,565
	<u>36,762,948</u>	<u>38,600,912</u>
	<u>\$ 37,781,298</u>	<u>\$ 39,660,217</u>

4. LONG TERM DEBT

	1977	1976
Bank loans due as stated hereunder	\$ 54,546,200	\$ 68,182,750
Less portion included in current liabilities (U.S. \$7,000,000) ...	* 6,818,275	6,818,275
Long term portion		
(1977 — U.S. \$49,000,000; 1976 — U.S. \$63,000,000)	47,727,925	61,364,475
Housing loans	1,123,181	898,373
	<u>\$ 48,851,106</u>	<u>\$ 62,262,848</u>
*Current portion as above	\$ 6,818,275	\$ 6,818,275
Add foreign exchange differential on U.S. \$7,000,000	811,725	251,725
Total as shown on statement of financial position	<u>\$ 7,630,000</u>	<u>\$ 7,070,000</u>

Repayment of the bank loans is secured by general assignments of the accounts and settlements receivable and by registered assignments under Section 88 of the Bank Act of all concentrates awaiting shipment and

mine supplies. The interest rate on these loans varies with the base rate for United States dollar loans made in Canada; the December 31, 1977 rate payable was 8½% per annum.

Under the terms of the bank loan agreement the Company is required to repay, on February 15 and August 15 in each of the years 1978 to 1981 inclusive, a principal amount equal to the lesser of 75% of the available cash flow as defined or U.S. \$7,000,000; any balance of the loans is due August 15, 1981.

5. CAPITAL STOCK

During the year 8,100 common shares were issued for \$70,129 cash under a Stock Option Plan.

At December 31, 1977, 33,700 common shares were reserved for issue under a Stock Option Plan. Options may be granted to employees of the Company or of Rio Algom Limited. Outstanding options have been granted to purchase 7,600 common shares at prices varying from \$7.20 to \$8.65 per share; these options expire on varying dates from April 16, 1979 to April 22, 1980.

Under the terms of the bank loan agreement dividends would be restricted if specified cumulative loan repayments have not been made or if the Company's working capital is not maintained at a minimum of \$20,000,000; to December 31, 1977 these specified loan repayments, totalling U.S. \$14,000,000, have been made.

6. COMMITMENTS AND CONTINGENT LIABILITIES

- (a) Rio Algom has agreed to supervise and manage the business of the Company until December 1, 1984. The 1977 management fee was \$476,000 and the fee for future years is \$500,000 per annum escalated in accordance with a formula based on published government indices and subject to a maximum based on a percentage of the earnings before taxes.
- (b) The Company has a contingent liability to buy back houses and mobile home lots at the Logan Lake townsite for \$5,692,541 until December 31, 1982.
- (c) Estimated total cost to complete approved capital expenditures at December 31, 1977 was approximately \$4,862,000 of which \$636,000 was committed.

7. ANTI-INFLATION PROGRAM

The Company is subject to and has complied with controls over prices, profit margins, compensation and dividends under the Canadian Government's Anti-Inflation Program.

8. REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

The aggregate direct remuneration paid or payable by the Company to the Directors and Senior Officers of the Company was \$297,660 in respect of the year ended December 31, 1977. In addition amounts, charged to earnings in prior years in respect of discretionary deferred bonus awards, totalling \$29,332 became payable to those individuals during 1977.

Supplementary Information

Five Year Review

Lornex Mining Corporation Ltd.

(\$000's omitted)

	1977	1976	1975	1974	1973
Net revenue from mine production	\$ 75,449	\$ 82,940	\$ 51,043	\$ 85,421	\$ 81,829
Investment and other income	1,495	1,503	842	4,059	831
	<u>76,944</u>	<u>84,443</u>	<u>51,885</u>	<u>89,480</u>	<u>82,660</u>
Operating costs	39,788	33,572	25,141	28,247	21,104
Administrative and general expense	7,564	6,913	5,677	6,342	4,763
Amortization and depreciation	9,072	8,002	5,917	7,029	8,366
	<u>56,424</u>	<u>48,487</u>	<u>36,735</u>	<u>41,618</u>	<u>34,233</u>
Operating profit	20,520	35,956	15,150	47,862	48,427
Interest expense	5,139	5,990	6,988	8,671	11,337
	<u>15,381</u>	<u>29,966</u>	<u>8,162</u>	<u>39,191</u>	<u>37,090</u>
Income and mineral resource taxes	7,600	14,063	7,536	16,510	5,192
Net earnings	<u>\$ 7,781</u>	<u>\$ 15,903</u>	<u>\$ 626</u>	<u>\$ 22,681</u>	<u>\$ 31,898</u>
Production Data:					
Tons of ore milled (000's)	17,065	17,016	12,893	16,445	13,987
— per operating day	46,753	46,877	38,259	45,056	38,320
Copper in concentrate (pounds — 000's) .	141,111	145,712	107,160	128,064	102,180
Molybdenum in concentrate (pounds — 000's)	3,795	3,769	3,084	4,038	3,481
Financial Data:					
Earnings per share	\$ 0.94	\$ 1.93	\$ 0.08	\$ 2.76	\$ 3.89
Long term debt (000's)	\$ 48,851	\$ 62,263	\$ 66,952	\$ 78,363	\$ 112,373
Shareholders' equity (000's)	\$ 89,194	\$ 81,343	\$ 65,238	\$ 64,538	\$ 41,848
— per share	\$ 10.80	\$ 9.86	\$ 7.93	\$ 7.86	\$ 5.09
Common shares outstanding (000's)	8,261	8,253	8,226	8,216	8,215
Capital expenditures (000's)	\$ 18,584	\$ 17,115	\$ 2,794	\$ 2,878	\$ 3,290

